

## **Consensus Economic Outlook**

The economic and revenue outlooks were agreed to at the January 13, 2005, Consensus Revenue Estimating Conference by the Administration, House Fiscal Agency, and Senate Fiscal Agency.

### **2004 U.S. Economic Review**

The current recovery is now over three years old, as dated by the National Bureau of Economic Research, having begun in November 2001. In 2004, real GDP is estimated to have grown by 4.4 percent, marking the third strongest annual growth in 20 years. Light vehicle sales have remained strong throughout the recovery, boosted by record incentives and low financing rates. Supported by historically low interest rates, new and existing home sales have remained strong as well.

Employment lagged the recovery and U.S. employment growth has been uneven. U.S. employment remains a quarter million jobs below its March 2001 peak. However, U.S. employment has grown each month for over a year and, during the past year, monthly employment growth averaged nearly 200,000 jobs a month.

The picture for manufacturing employment has been considerably less upbeat. Beginning in August 2000, manufacturing employment declined 42 straight months. While manufacturing reported solid gains in early 2004, manufacturing employment has remained essentially unchanged in recent months. Rapid productivity gains allowed firms to reduce payroll employment even as they continued to increase output.

Interest rates have remained at historically low levels. However, in the light of a strengthening economy and inflationary pressures, the Federal Reserve increased the target federal funds rate from 1.0 percent to 2.25 percent over the course of 2004. The Federal Reserve indicated it would continue to increase rates at a “measured” pace. Inflationary pressures will build with higher commodity prices and higher wages as job growth increases. Energy prices, most notably oil, have increased due to a restricted supply and growing world demand. Security concerns for oil supplies are also in the forefront with tensions high in Iraq and other oil producing nations.

Federal government expenditures continued to report solid gains in 2004. However, state and local government expenditures rose only slightly last year. The international trade deficit continued to worsen over the course of 2004. In the light of large federal budget and international capital account deficits, the value of the U.S. dollar weakened considerably. The stock market registered solid gains with the S&P 500 index up 9.0 percent for the year.

Over the past few years, imports and transplants have continued to increase their market share. The traditional Big Three market share has continued to fall, with their share at

58.7 percent for 2004, a record low. In 2004, U.S. vehicle production declined 0.9 percent while Michigan vehicle production fell 6.7 percent.

The index of leading economic indicators suggests that growth will moderate in the near future. The index declined five straight months before increasing in November and December.

### **2004 Michigan Economic Review**

Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Given extremely weak manufacturing employment performance, declining vehicle production, declines in Big 3 market share and continued supply rationalization among vehicle suppliers, Michigan's employment performance has been below the national average. Substantial productivity gains in the vehicle industry have also contributed to Michigan's sub-par employment performance. In 2004, Michigan wage and salary employment is estimated to have declined by 1.1 percent, marking the fourth straight year that Michigan employment has fallen. From Michigan's employment peak in June 2000 compared to December 2004, Michigan has lost 344,400 jobs. By this time after the 1990-1991 recession, Michigan employment had risen by about 200,000 jobs *above* its pre-recession peak.

In 2004, Michigan's unemployment rate fell to an estimated 6.7 percent. Michigan personal income is expected to have risen 2.7 percent; wages and salaries income is expected to have grown by 0.7 percent.

### **2005 and 2006 U.S. Consensus Economic Outlook**

Real GDP is forecast to grow 3.2 percent in both 2005 and 2006, down from an estimated 4.4 percent growth rate in 2004 (See Table L-1). High levels of productivity, business investment, and an improving job market will help support growth. The end of bonus depreciation, deficit constrained federal spending and rising interest rates will mute growth.

Light vehicle sales are forecast to be 16.8 million units in both 2005 and 2006. Inflation is projected to remain moderate at 2.6 percent and 2.4 percent in 2005 and 2006, respectively. Interest rates are forecast to continue to rise but still remain at historically low levels.

The U.S. unemployment rate is projected to remain relatively stable over the next two years with a 5.4 percent unemployment rate in 2005 and a 5.5 percent rate in 2006.

## **2005 and 2006 Michigan Consensus Economic Outlook**

Michigan wage and salary employment is forecast to increase slightly in 2005 and post more moderate gains in 2006. After four straight years of decline, wage and salary employment is projected to rise 0.3 percent in 2005 and 1.0 percent in 2006.

Michigan's unemployment rate is forecast to rise slightly to 6.9 percent in 2005 before declining to 6.8 percent in 2006.

Michigan personal income is forecast to increase 4.5 percent in 2005, up from the estimated 2.7 percent increase in 2004. In 2006, personal income is estimated to increase 5.6 percent. Inflation, as measured by the Detroit CPI, is forecast to be 2.4 percent in 2005 and 2.2 percent in 2006. As a result, real Michigan personal income (inflation adjusted) is expected to rise 2.0 percent in 2005 and 3.3 percent in 2006.

In FY 2005, Michigan wages and salaries are expected to grow by 2.5 percent and then accelerate to 4.0 percent growth in FY 2006. Disposable income is expected to rise 3.4 percent in 2005 and 5.0 percent in 2006. The inflation rate is expected to remain moderate at 2.6 percent in FY 2005 and 2.1 percent in FY 2006.

### **Forecast Risks**

If businesses and/or consumers lose confidence in the expansion, both national and Michigan employment growth may be slower than forecast. If employment gains do not materialize, economic growth will decline as consumer and business spending retrenches. In large part, Michigan employment is still declining. If Michigan's employment level does not begin to increase soon, state economic growth will be below forecast levels.

Compared to other states, sharp declines in Big 3 market share would affect the Michigan economy adversely. Similarly, faster productivity growth may decrease employment and overall economic growth. Consumer debt levels, coupled with higher interest rates, also pose a risk.

Continued higher oil and natural gas prices could curb growth by reducing consumers' discretionary income and increasing production costs. Weaker growth abroad could also slow domestic growth as exports decline. If the U.S. dollar declines sharply, inflation risks would increase and financial markets may be shaken. Geopolitical concerns continue to pose a risk to the forecast.

**Table L-1**  
**Consensus Economic Forecast**  
January 2005

|   | Calendar<br>2003<br>Actual | Calendar<br>2004<br>Forecast | Percent<br>Change<br>from Prior<br>Year | Calendar<br>2005<br>Forecast | Percent<br>Change<br>from Prior<br>Year | Calendar<br>2006<br>Forecast | Percent<br>Change<br>from Prior<br>Year |
|---|----------------------------|------------------------------|---|------------------------------|---|------------------------------|---|
| <b>United States</b>  |                            |                              |   |                              |   |                              |   |
| Real Gross Domestic Product<br>(Billions of Chained 2000 Dollars) | \$10,381                   | \$10,838                     | 4.4%                                    | \$11,185                     | 3.2%                                    | \$11,540                     | 3.2%                                    |
| Implicit Price Deflator GDP<br>(2000 = 100)                       | 106.0                      | 108.2                        | 2.1%                                    | 110.6                        | 2.2%                                    | 113.1                        | 2.3%                                    |
| Consumer Price Index<br>(1982-84 = 100)                           | 184.0                      | 189.0                        | 2.7%                                    | 193.9                        | 2.6%                                    | 198.6                        | 2.4%                                    |
| Personal Consumption Deflator<br>(2000 = 100)                     | 105.5                      | 107.7                        | 2.1%                                    | 109.9                        | 2.0%                                    | 112.1                        | 2.0%                                    |
| 3-month Treasury Bills<br>Interest Rate (percent)                 | 1.0                        | 1.4                          |   | 2.4                          |   | 3.6                          |   |
| Aaa Corporate Bonds<br>Interest Rate (percent)                    | 5.7                        | 5.6                          |   | 5.7                          |   | 6.4                          |   |
| Unemployment Rate - Civilian<br>(percent)                         | 6.0                        | 5.5                          |   | 5.4                          |   | 5.5                          |   |
| Light Vehicle Sales<br>(millions of units)                        | 16.6                       | 16.7                         | 0.5%                                    | 16.8                         | 0.6%                                    | 16.8                         | 0.0%                                    |
| Passenger Car Sales<br>(millions of units)                        | 7.6                        | 7.4                          | -2.8%                                   | 7.4                          | 0.0%                                    | 7.5                          | 1.4%                                    |
| Light Truck Sales<br>(millions of units)                          | 9.0                        | 9.3                          | 3.2%                                    | 9.4                          | 1.1%                                    | 9.3                          | -1.1%                                   |
| Import Share of Light Vehicles<br>(percent)                       | 19.9                       | 20.1                         |   | 20.6                         |   | 21.1                         |   |
| <b>Michigan</b>   |                            |                              |   |                              |   |                              |   |
| Wage and Salary Employment<br>(thousands)                         | 4,412                      | 4,363                        | -1.1%                                   | 4,376                        | 0.3%                                    | 4,420                        | 1.0%                                    |
| Unemployment Rate<br>(percent)                                    | 7.3                        | 6.7                          |   | 6.9                          |   | 6.8                          |   |
| Personal Income<br>(millions of dollars)                          | \$314,460                  | \$322,950                    | 2.7%                                    | \$337,483                    | 4.5%                                    | \$356,382                    | 5.6%                                    |
| Real Personal Income<br>(millions of 1982-84 dollars)             | \$172,307                  | \$173,816                    | 0.9%                                    | \$177,342                    | 2.0%                                    | \$183,230                    | 3.3%                                    |
| Wages and Salaries<br>(millions of dollars)                       | \$176,493                  | \$177,728                    | 0.7%                                    | \$184,304                    | 3.7%                                    | \$192,155                    | 4.3%                                    |
| Detroit Consumer Price Index<br>(1982-84 = 100)                   | 182.5                      | 185.8                        | 1.8%                                    | 190.3                        | 2.4%                                    | 194.5                        | 2.2%                                    |
| Detroit CPI Fiscal Year<br>(1982-84 = 100)                        | 182.0                      | 184.4                        | 1.3%                                    | 189.2                        | 2.6%                                    | 193.2                        | 2.1%                                    |